

Decision _____

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of PACIFIC GAS AND ELECTRIC COMPANY to issue, sell, and deliver one or more series of Debt Securities and to guarantee the obligations of others in respect to the issuance of Debt Securities, the total aggregate principal amount of such long-term indebtedness and guarantees not to exceed \$3.0 billion; to execute and deliver one or more indentures; to sell, lease, assign, mortgage, or otherwise dispose of or encumber utility property; to issue, sell and deliver in one or more series, cumulative Preferred Stock -- \$25 Par Value, Preferred Stock -- \$100 Par Value, Preference Stock or any combination thereof; to utilize various debt enhancement features; enter into interest rate hedges; and for an exemption from the Commission's Competitive Bidding Rule.

(U 39 M)

Application 06-02-005
(Filed February 6, 2006)**OPINION AUTHORIZING THE ISSUANCE
OF DEBT AND PREFERRED STOCK****I. Summary**

This opinion grants Pacific Gas and Electric Company (PG&E) the authority to issue \$3 billion of Debt Securities consisting of long-term debt and preferred stock, as requested in Application (A.) 06-02-005. This opinion also authorizes PG&E to: encumber utility property, including its accounts receivable, to secure Debt Securities; enter into interest-rate caps, collars, swaps, hedges, and other financial instruments (collectively hedges) subject to the conditions

enumerated in the body of this opinion; exempt certain Debt Securities from the Commission's Competitive Bidding Rule as enumerated in the body of this order; exclude credit enhancements that do not increase the amount of debt owed by PG&E from the determination of its outstanding debt; and, report all Debt Securities information required by General Order (GO) 24-B to the Commission on a quarterly basis.

II. Request

PG&E seeks authorization to issues \$3.0 billion of Debt Securities, including preferred stock, until the aggregate principal amount authorized has been fully utilized. PG&E intends to utilize debt enhancement features to improve the terms and conditions of the Debt Securities and to lower its overall cost of money for the benefit of its ratepayers. As detailed in its application, these enhancement features include credit enhancements, redemption provisions, put options, sinking funds, tax-exempt financing, and warrants.

PG&E also seeks authorization to utilize its accounts receivable to secure Debt Securities and hedges to manage interest rate risk. Finally, PG&E seeks an exemption from the Commission's Competitive Bid Rule and modification to the GO 24-B Debt Securities reporting requirement.

III. Discussion

The principal amount, form and terms and conditions of each series of Debt Securities will be determined by PG&E's board of directors or management according to market conditions at the time of sale or issuance. The Debt Securities may bear a fixed, floating or variable rate of interest and may be issued at par or with an original issue discount or premium. The Debt Securities will be issued with maximum maturities of 49 years for first and refunding mortgage bonds and 49 years for debentures, notes, preferred securities, and credit or loan

agreements. Preferred securities may have either mandatory or optional redemption features. PG&E may issue Debt Securities directly or may issue them through an affiliate that will in turn lend or otherwise transfer the proceeds to or for the benefit of PG&E.

The types of Debt Securities that PG&E proposes to issue are similar to those authorized in Decision (D.) 04-10-037, dated October 28, 2004. These Debt Securities detailed in PG&E's application consist of:

1. Secured Debt Securities in the form of First Mortgage Bonds.
2. Unsecured Debt Securities such as debentures and notes.
3. Overseas Indebtedness sold to foreign investors that would be denominated in U.S. dollars or foreign currencies.
4. Preferred Securities issued by a subsidiary.
5. Foreign Currency Denominated Securities.
6. Medium-term Notes.
7. Direct Loans obtained from financial institutions such as banks and insurance companies.
8. Accounts Receivable Financing.
9. Variable-Rate Debt based on short-term interest rate indices, bankers' acceptances, PG&E's credit ratings, or other factors.
10. Preferred Stock.

The Commission authorized most of PG&E's current debt in D.04-01-024 to finance PG&E's emergence from bankruptcy. PG&E is currently authorized to issue \$14.9 billion of long-term debt and equity as shown in its March 2, 2006 supplement to the application. Pursuant to D.04-01-024, PG&E issued \$6.4 billion of First Mortgage Bonds with \$0.4 billion remaining to be issued.

PG&E fully issued its authorized \$0.2 billion of preferred stock and \$8.3 billion of common stock as of September 30, 2005.¹

PG&E used a long-term forecast covering the five year period beginning January 1, 2006 and ending December 31, 2010 to determine its future financing needs. The forecast includes uses of funds such as capital expenditures and maturing debt obligations, as well as sources of funds such as cash flow from operations. The result of this forecast is set forth in its March 2, 2006 supplemental filing.

The current forecast of annual capital expenditures averages approximately \$2.5 billion over the forecast period. These expenditures include infrastructure replacements and upgrades to gas and electric transmission and distribution facilities, upgrades to its retained generation assets, investment in new generation facilities, and PG&E's advanced metering infrastructure initiative.² Not included in the forecast are additional generation facilities that PG&E may build rather than acquiring through power purchase contracts, or expansion of its gas pipeline infrastructure to connect to new gas supplies such as liquefied natural gas.

PG&E's \$0.4 billion authorized long-term debt remaining to be issued is insufficient to meet its ongoing capital spending requirements, replace maturing debt, and redeem debt and preferred stock. Hence, PG&E seeks authorization to issue \$3.0 billion of Debt Securities.

¹ Schedule XI-A, Supplemental Financial Information Filing, dated March 2, 2006.

² This is a \$1.5 billion project to automate all nine million of PG&E's gas and electric meters as requested by PG&E in A.05-06-028.

PG&E expects that approval of its Debt Securities request will provide it with sufficient flexibility to meet its financial and service obligations. PG&E expects that it will not use more than \$2.4 billion of the proposed financing proceeds for construction expenditures and acquisition of property or to reimburse PG&E for money it has expended for those purposes. The remaining \$600 million of proposed financing proceeds is expected to be used for the retirement or refunding of securities previously issued.

A. Approval

PG&E's request to issue Debt Securities, including preferred stock, is subject to §§ 816, *et seq.* of the Public Utilities Code.³ The Commission has broad discretion under §§ 816, *et seq.* to determine if a utility should be authorized to issue debt and preferred stock. Where necessary and appropriate, the Commission may attach conditions to the issuance of debt and preferred stock to protect and promote the public interest.

1. Issuance of Debt Securities

PG&E has substantiated that its \$3.0 billion Debt Securities request is necessary to satisfy its 2006 -2010 needs for financing capital expenditures, acquiring property, and retiring or refunding securities. These purposes are authorized by § 817 and, as required by § 818, are not reasonably chargeable to operating expenses or income. Therefore, we will grant PG&E authority under § 816, *et seq.* to issue to \$3.0 billion of long-term debt and preferred stock for the aforementioned purposes, as detailed in the application.

Consistent with § 824, PG&E shall maintain records to identify the specific long-term debt and preferred stock issued pursuant to this Opinion, and

³ All statutory references are to the Public Utilities Code unless otherwise stated.

demonstrate that proceeds from such debt and preferred stock have been used only for the purposes authorized by today's Opinion.

PG&E may allocate the authorized debt and preferred stock among the authorized purposes as PG&E deems necessary. PG&E may also issue any combination of long-term debt and preferred stock, as long as the total amount issued pursuant to this Opinion does not exceed \$3.0 billion.

2. Encumbrance of Utility Property

PG&E seeks authority to use its accounts receivable to secure Debt Securities. PG&E anticipates that such transactions would be structured as a true sale for bankruptcy purposes and debt for financial reporting and tax purposes, although other structures may be developed using accounts receivable as security or collateral.

This request to encumber utility property is subject to § 851 which states, in relevant part, that no utility shall encumber any part its plant, system, or other property necessary or useful in the performance of its duties to the public, or any franchise or permit or right there-under without first having secured from the commission an order authorizing it to do so.

Consistent with previous Commission decisions, we will authorize PG&E to encumber its accounts receivables to improve the terms and conditions of the Debt Securities and to lower PG&E's overall cost of money for the benefit of ratepayers.⁴

3. Hedging Requirements

PG&E seeks authority to use hedges to manage interest rate risk, as detailed in its Application. PG&E also requests that these hedges not be counted

⁴ See, for example, D.05-04-003 (2005) *mimeo.*, p. 10, Ordering Paragraph 4.

against its authorized debt, since these hedges would not affect the amount of the underlying debt issued.

The terms and conditions of hedges will be determined by PG&E based on market conditions at the time such transactions are negotiated. PG&E will enter into these hedging contracts only when a future financing is clearly required, such as replacement of a maturing issue.

PG&E proposes to comply with the following restrictions regarding hedging transactions entered into pursuant to this Application:

1. Separately report all interest income and expense (as recorded for ratemaking purposes) arising from all hedging transactions in its regular report to the Commission.
2. Hedging transactions will not exceed at any time 20 % of PG&E's total long-term debt outstanding.
3. All costs associated with hedging transactions shall be subject to review in PG&E's cost of capital proceedings or other appropriate proceedings.
4. Hedging transactions carrying potential counterparty risk must have counterparties with investment grade credit ratings.
5. PG&E will provide the following available to Commission staff within 30 days of a request: (i) all terms, conditions, and other details of hedge transactions; (ii) rationale for the hedge transactions; (iii) estimated costs for the "alternative" or unhedged transactions; and (iv) copy of the hedge agreements and associated documentation.

Consistent with previous Commission decisions,⁵ we will authorize PG&E to use hedges subject to the above agreed upon conditions. We also

conditionally grant PG&E's request to not count hedges as outstanding debt.⁶ Specifically, we will not count hedges against PG&E's authorized debt to the extent the hedges are both recorded as a liability in accordance with generally accepted accounting principles (GAAP), and deemed effective under GAAP in offsetting changes to the fair value or cash flows of the risks being hedged. On the other hand, hedges will be counted against PG&E's authorized debt to the extent they are recorded as liability in accordance with GAAP, but are not deemed effective under GAAP in offsetting changes to the fair value or cash flows associated with the risks being hedged.

4. Competitive Bidding Rule Exemption

Resolution No. F-616, issued on October 1, 1986, requires utilities to issue debt using competitive bids. The purpose of this requirement, known as the Competitive Bidding Rule, is to reduce the cost of debt issued by utilities. The Resolution also provides for utilities to seek an exemption from the Competitive Bidding Rule for debt issues in excess of \$200 million. An exemption request will only be granted upon a compelling showing by a utility that because of the size of the issues, an exemption is warranted.

PG&E seeks an exemption from the Competitive Bidding Rule on the basis that:

1. Competitively bidding larger issues may result in higher costs due to the fragmenting of the investment banking community into competitive

⁵ See, for example, D.95-09-023, D.96-05-066, and D.03-12-004.

⁶ Consistent with D.02-11-030, Footnote 13, any debt issued by PG&E as part of a transaction involving an interest-rate swap shall be used to determine the amount of authorized and outstanding debt.

bidding syndicates and the increased risk thereby assumed by each of them.

2. The competitive bidding process is fundamentally designed for highly rated, well-known issuers who do not need to avail themselves of the opportunities for communicating to, and receiving market intelligence from, the investment community in order to achieve a successful offering.
3. Competitive bidding may leave PG&E limited and undesirable options for obtaining needed financing.

PG&E requests that the following Debt Securities also be exempted from the Competitive Bidding Rule because they are typically issued through negotiated arrangements: notes sold through a placement agent on a reasonable efforts basis; trust preferred securities; accounts receivable financings; overseas indebtedness; foreign currency securities; notes; tax-exempt securities, and interest-rate hedges. However, it will, pursuant to the Competitive Bidding Rule, offer through competitive bidding other fixed-rate Debt Securities in the form of First and refunding mortgage bonds, intermediate and long-term notes, and debentures of \$200 million or less in principal amount (other than tax-exempt securities) that are sold publicly in the domestic market.

To provide added flexibility to take advantage of market opportunities, PG&E requests that the Commission modify the Competitive Bidding Rule to permit PG&E to use the following procedures for those situations where the Rule remains applicable:

1. To shorten the time between the issuance of an invitation for bids and the scheduled receipt of bids to a period which is the shortest time reasonably required to obtaining a sufficient number of bids from underwriters or purchasers or groups thereof.

2. To accelerate, postpone, or cancel the scheduled date and time for receipt of bids.
3. To reject all bids submitted.
4. To request the resubmission of bids.
5. To reschedule subsequent receipt of bids.
6. To vary the amount, terms, and conditions of the Debt Securities submitted for bids.
7. To waive the requirement for newspaper publication of the above items.

PG&E's request for the previously described exemptions from, and modifications to, the Competitive Bidding Rule is granted on the basis that the Commission has routinely granted PG&E and other utilities similar exemptions and modifications⁷ with no discernable adverse impacts on the utilities, their customers, or the public at large; and on PG&E's representation that granting the exemptions and modifications will enable it to obtain debt in a manner advantageous to PG&E and its ratepayers. We make no finding regarding the reasonableness of the rates, terms, and conditions of debt issued by PG&E pursuant to the exemptions and modifications granted herein.

5. Reporting Requirement

GO 24-B requires utilities to submit a monthly report to the Commission that contains, among other things: (i) the amount of debt and preferred stock issued by the utility during the previous month; (ii) the total amount of debt and preferred stock outstanding at the end of the prior month; (iii) the purposes for which the utility expended the proceeds realized from the

⁷ See, for example, D.04-10-037 (2004) *mimeo.*, pp. 50-51; and D.03-12-004, *mimeo.*, pp. 32-33.

issuance of debt and preferred stock during the prior month; and (iv) a monthly statement of the separate bank account that the utility is required to maintain for all receipts and disbursements of money obtained from the issuance of debt and preferred stock.

PG&E seeks authority to report quarterly, instead of monthly, the information required by GO 24-B in order to reduce its administrative cost of complying with the GO and to conform to past practice. This reporting request is reasonable and consistent with past Commission practice.⁸ PG&E may report quarterly to the Commission the information required by GO 24-B.

IV. Fee

PG&E requests that it be charged a fee on only \$2.4 billion of its \$3.0 billion debt authorization requested. This is because PG&E intends to use the remaining \$600 million of its requested debt instruments to retire or refund securities previously issued. However, if PG&E actually uses any of the \$600 million earmarked for other than the retirement or refund of securities previously issued it will notify the Commission in writing and pay the corresponding fee.

Whenever the Commission authorizes a utility to issue debt and preferred stock, the Commission is required to charge and collect a fee pursuant to §§ 1904(b) and 1904.1. A fee is not applicable on any such issues used to guarantee, take over, refund, discharge, or retire any stock, bond, note, or other evidence of indebtedness on which a fee has theretofore been paid to the Commission. (§ 1904.1.)

⁸ See, for example, D.04-10-037 (2004) *mimeo.*, p. 51; and, D.03-12-052 (2003) *mimeo.*, pp. 11-12.

PG&E shall remit the required \$1.206 million fee to the Commission's Fiscal Office.⁹ If PG&E uses any of the \$600 million for purposes other than the retirement or refund of securities previously issued, it shall notify the Commission in writing and pay the appropriate fee.

V. California Environmental Quality Act

Under the California Environmental Quality Act (CEQA) and Rule 17.1 of the Commission's Rules of Practice and Procedure (Rules), we must consider the environmental consequences of projects that are subject to our discretionary approval.¹⁰ Thus, we must consider whether approval of this application will alter an approved project, result in new projects or change operations in ways that have an environmental impact.

PG&E expects that it will not use more than \$2.4 billion of the proposed financing proceeds for construction expenditures and acquisition of property or to reimburse PG&E for money it has expended for those purposes. This decision does not authorize any capital expenditures or construction projects. To the extent capital expenditures are financed with the proceeds of the long-term debt and preferred stock issued pursuant to this decision, CEQA review should occur as needed through the regulatory processes applicable to each capital project.

⁹ The fee is assessed on \$2.4 billion of authorized Debt Securities as follows: (\$2 times (\$1,000,000/\$1,000) plus (\$1 times \$9,000,000/\$1,000 plus \$0.5 times \$2,390,000,000/\$1,000 equals \$1.206 million. The remaining \$600 million of the total \$3.0 billion Debt Securities being authorized is excluded from the fee calculation to the extent PG&E uses that debt to retire and refund securities previously charged a fee.

¹⁰ Pub. Resources Code Section 21080.

VI. Category and Need for Hearings

PG&E requested that this matter be categorized as ratesetting. By Resolution ALJ 176-3167, dated February 16, 2006, the Commission preliminarily determined that this was a ratesetting proceeding and that a hearing would not be necessary.

Notice of the application appeared in the Commission's Daily Calendar of February 8, 2006. There were no protests to the application. Based on the record, we affirm that this is a ratesetting proceeding, and that a hearing is not necessary.

VII. Waiver of Comment Period

This is an uncontested matter in which the decision grants the relief requested. Therefore, the otherwise applicable 30-day period for public review and comment is being waived, pursuant to § 311(g) (2).

VIII. Assignment of Proceeding

John A. Bohn is the Assigned Commissioner and Michael J. Galvin is the assigned ALJ in this proceeding.

Findings of Fact

1. PG&E requests authority to issue \$3 billion of Debt Securities.
2. There were no protests to this application.
3. PG&E supplemented its application with financial information to support its request to issue additional Debt Securities.
4. PG&E has a reasonable need to issue \$3.0 billion of long-term debt and preferred stock during 2006 – 2010 to finance capital expenditures, replace maturing debt, and redeem debt and preferred stock.
5. PG&E requests authority under § 851 to issue First and refunding mortgage bonds and to use its accounts receivable to secure its debt.

6. PG&E requests authority to issue many different types of Debt Securities and preferred stock using a wide variety of means.

7. PG&E requests that credit enhancements not be counted against its authorized debt.

8. PG&E requests authority to use hedges to manage the risks associated with interest rate volatility. PG&E also requests that its use of these financial instruments not be counted against its authorized debt.

9. Resolution F-616 requires utilities to issue debt using competitive bids. The Resolution also provides for exemptions from the Competitive Bidding Rule for debt issues in excess of \$200 million and debt that must be obtained on a negotiated basis such as variable-rate debt.

10. PG&E represents that granting the requested exemptions from, and modifications to the Competitive Bidding Rule will enable PG&E to obtain debt in a manner that is advantageous to PG&E and its ratepayers.

11. GO 24-B requires utilities to submit a monthly report to the Commission that contains, among other things: (i) the amount of debt and preferred stock issued by the utility during the previous month; (ii) the total amount of debt and preferred stock outstanding at the end of the prior month; (iii) the purposes for which the utility expended the proceeds realized from the issuance of debt and preferred stock during the prior month; and (iv) a monthly statement of the separate bank account that the utility is required to maintain for all receipts and disbursements of money obtained from the issuance of debt and preferred stock.

12. To minimize administrative costs, PG&E requests permission to report to the Commission on a quarterly basis all the information required by GO 24-B for any debt and preferred stock issued by PG&E pursuant to this Opinion.

13. The Commission has routinely authorized utilities to report on a quarterly basis the information required by GO 24-B in order to reduce the utilities' administrative and compliance costs.

14. A.06-02-005 does not propose, and today's Opinion does not authorize, any specific new construction or changes in use of existing assets and facilities.

15. Notice of A.06-02-005 appeared in the Commission's Daily Calendar. There were no protests or other responses to A.04-05-041.

16. In Resolution ALJ 176-3135 issued on June 9, 2004, the Commission preliminarily determined that this proceeding should be categorized as ratesetting and that hearings would not be necessary.

Conclusions of Law

1. This is a ratesetting proceeding.
2. There is no need for hearings.
3. The application should be granted as requested.
4. The authority granted by this Opinion should not become effective until PG&E has paid the fees prescribed by §§ 1904(b) and 1904.1.
5. PG&E should not use the proceeds from the debt and preferred stock authorized by this Opinion to fund capital projects until PG&E has obtained any required Commission approvals for the projects, including any required environmental review under CEQA.
6. The following Order should be effective immediately so that PG&E may issue as soon as possible the debt and preferred stock authorized herein.

O R D E R**IT IS ORDERED** that:

1. Pacific Gas and Electric Company (PG&E) is authorized to issue \$3.0 billion of new long-term debt and preferred stock to finance capital expenditures, replace maturing debt, and to redeem debt and preferred stock.
2. PG&E may encumber utility property, including accounts receivables, to secure Debt Securities authorized by this order.
3. PG&E may guarantee the Debt Securities of regulated direct or indirect subsidiaries or affiliates of PG&E or of government entities that issue Debt Securities on behalf of PG&E.
4. Credit enhancements authorized by this Order shall not count against the amount of debt authorized by this Order so long as there is no possibility that such credit enhancements will ever increase the amount of PG&E's debt obligations.
5. PG&E may enter into interest-rate caps, collars, swaps, hedges, and other financial instruments to manage interest rate risks (collectively, "hedges") to the extent that PG&E complies with the conditions enumerated in the body of this Order.
6. The following types of debt issued by PG&E pursuant to this Order are exempt from the Competitive Bidding Rule set forth in Resolution F-616: debt with a principal amount greater than \$200 million, variable-rate debt securities; notes sold through a placement agent on a reasonable efforts basis; trust preferred securities; accounts receivable financings; overseas indebtedness foreign currency securities; notes; tax-exempt securities; and, hedges.
7. PG&E is authorized to do the following in those situations where the Competitive Bidding Rule remains applicable:

- i. To shorten the time between the issuance of an invitation for bids and the receipt of bids to a period that is the shortest time reasonably required to obtain a sufficient number of bids from underwriters, purchasers, or groups thereof.
 - ii. To accelerate, postpone, or cancel the scheduled date and time for receipt of bids.
 - iii. To reject all bids submitted.
 - iv. To request the resubmission of bids.
 - v. To reschedule subsequent receipt of bids.
 - vi. To vary the amount, terms, and conditions of the Debt Securities submitted for bids.
 - vii. To waive the requirement for newspaper publication of the above items.
8. PG&E shall provide compelling evidence to substantiate future exemption requests from the competitive bidding rule.
9. PG&E may report on a quarterly basis all the information required by General Order 24-B with respect to debt and preferred stock issued pursuant to this Order.
10. PG&E shall remit to the Commission's Fiscal Office a check for \$1.206 million as required by § 1904(b) of the Public Utilities Code. The decision number of this Order shall appear on the face of the check.
11. The authority granted by this Order shall not become effective until PG&E remits \$1.206 million to the Commission's Fiscal Office.
12. PG&E shall comply with all applicable environmental laws and regulations when planning and implementing any capital expenditure programs that are financed, in whole or in part, with the proceeds from the debt and preferred stock authorized by this Order.

13. Application 06-02-005 is closed.

This order is effective today.

Dated _____, at San Francisco, California.